

Before the
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Rule on Motions Concerning
Mail Preparation Changes

Docket No. RM2016-13

PUBLIC REPRESENTATIVE COMMENTS

(October 17, 2016)

I. INTRODUCTION

The Public Representative hereby submits comments on the Commission's Notice of Proposed Rulemaking issued September 9, 2016 in this proceeding.¹ The Notice proposes to amend the Commission's rules to conform to "changes to its rules that specifically define or describe attributable costs, pursuant to Commission Order No. 3506."²

II. BACKGROUND

The Notice proposes to amend section 3015.7 of the Commission's rules, 39 CFR 3015.7, to provide that attributable costs must be expanded to include inframarginal costs calculated as part of a competitive product's incremental costs (in addition to a product's volume-variable costs and product-specific fixed costs). Notice at 4.

Also, because the definition of attributable costs is expanded to include inframarginal costs calculated as part of a competitive product's incremental costs, the rule defining the test for cross-subsidies when incremental cost data is *not* available is

¹ Notice of Proposed Rulemaking on Changes Concerning Attributable Costing, September 9, 2016 (Notice).

² Docket No. RM2016-2, Order Concerning United Parcel Service, Inc.'s Costing Methodologies (UPS Proposals One, Two, and Three), September 9, 2016 (Order No. 3506) at 124.

proposed to be modified by revising section 3015.7(a). Notice at 5. The test for cross-subsidies will no longer be attributable costs supplemented with causally related group-specific costs. Rather, the test for cross-subsidies in section 3015.7 will be the sum of competitive products' volume-variable costs and product-specific costs supplemented to include causally related, group-specific costs. Notice at 8.

The Notice also states that while these are the only rules under title 39 requiring revisions as a result of Order No. 3506, the finding concerning incremental costs “applies to any reference of attributable costs in title 39 unless otherwise indicated by the rules.” Notice at 6, citing generally Order No. 3506. Thus, the Commission has stated that, unless otherwise indicated, the findings in Order No. 3506 concerning incremental costs are to be applied or interpreted as a rule wherever the term attributable cost appears in title 39.

III. DISCUSSION

A. The Proposed Amendments Appear to Conform to Order No. 3506

The Commission proposes to amend three of its rules: 39 CFR § 3015.7, § 3060.10, and § 3060.21. The proposed revision to Part 3015 amends § 3015.7 pertaining to the regulation of rates for competitive products. Section 3015.7 provides rules for “Standards for compliance” with 39 U.S.C. § 3633, and the revision would alter the standards. The other two proposed amendments make conforming changes to revise Part 3060 of 39 CFR pertaining to Accounting Practices and Tax Rules for the Theoretical Competitive Products Enterprise previously established pursuant to 39 U.S.C. §§ 2011 and 3641. The revision of section 3060.10 revises costing provisions. The revision of section 3060.21 adds an additional line to the Income Report, Table 1, to include “Incremental Inframarginal Costs.”

The proposed rules appear to conform to the Commission’s finding and directive in Order No. 3506. However, the Notice does not explain the Commission’s meaning or

understanding of the phrase in section 3015.7(a) eliminating some attributable costs (as defined) from the test for cross-subsidies “to the extent that incremental cost data are unavailable.” Some discussion would be useful to forestall potential attempts to game the outcome by defining or redefining “unavailable.”

B. Revision of Commission regulations pursuant to 39 U.S.C. § 3633 requires compliance with Section 703(d) of the PAEA

1. Docket No. RM2016-2

In effect, the rules proposed in this proceeding appear to be merely ministerial in nature, intended only to carry out the findings of Order No. 3506 in Docket No. RM2016-2.

Docket No. RM2016-2 was initiated pursuant to 39 U.S.C. § 2652 to consider two proposals by United Parcel Service, Inc. (UPS). In Proposal One, UPS proposed to add certain inframarginal costs to the calculation of Postal Service attributable costs of products. Order No. 3506 at 15. Proposal Two considered whether a significant portion of institutional costs classified as fixed include variable costs which should be attributed to products. *Id.* at 62. The Commission’s order rejected both of the UPS proposals. *Id.* at 125. The Commission declined to review a third proposal but will at a later time conduct a similar review as required by section 3336(b). *Id.* However, Order No. 3506 adopted for the first time the incremental cost methodology to determine class-level and product-level attributable costs. *Id.*

In Docket No. RM2016-2, the Public Representative’s Comments³ pointed out that subsection (d) of uncodified section 703 of the PAEA requires that the Commission, when revising regulations under section 3633, must take into account events that have occurred subsequent to the recommendations in the Federal Trade Commission’s (FTC) section 703 Report which affect the continuing validity of the FTC’s estimate of the net

³ Docket No. RM2016-2, Public Representative Comments, January 27, 2016 (Public Representative Comments). See *also*, Public Representative Reply Comments, March 25, 2016.

economic effect of the laws that apply differently to the Postal Service than to private companies.⁴

The Report was required by section 703(a) to be completed within 1 year after the date of enactment of the PAEA.⁵ Section 703(b) required the Report to include recommendations to bring the effects of such differences in the laws to an end and, “in the interim, to account under section 3633 of title 39, United States Code (as added by this Act), for the net economic effects provided by those laws.” Section 703(d) places a requirement on the Commission to consider subsequent events affecting the validity of the FTC’s estimate when revising its regulations under 39 U.S.C. § 3633. Note that both subsections 703(b) and 703(d) refer to the whole of section 3633, not any individual subsection of section 3633.

Order No. 3506 summarized the comments of the Public Representative and others about section 703 regarding the conditions in the competitive product market. Order No. 3506 at 109-117. Without analyzing the comments, or ruling on the arguments of the participants in response to the comments, the Commission concluded that its review was not subject to section 703 of the PAEA. *Id.* at 117-122. It stated, “Accordingly, the Commission finds that the analytical principles are regulations promulgated and revised under section 3652, not section 3633.” *Id.* at 121. It concluded that its order was not revising Commission regulations, but is an action pursuant to 39 U.S.C. § 3652: “For the reasons stated above, neither Proposal One nor Proposal Two seek to promulgate or revise regulations required under 39 U.S.C. § 3633.” Order No. 3506 at 122. Although it rejected Proposals One and Two, it ruled that attributable costs must include inframarginal costs calculated as part of a competitive product’s incremental costs.

⁴ Public Representative Comments at 7, 43-53; Public Representative Reply Comments, March 25 2016 at 28..

⁵ Federal Trade Commission, Accounting for Laws that Apply Differently to the United States Postal Service and its Private Competitors, December 2007 (FTC Report).

Order No. 3506 sought to distinguish proceedings under section 3652 involving changes in analytical principles that may improve the quality, accuracy, or completeness of data included in periodic reports, from proceedings under section 3633 which, it said, are intended to ensure the Postal Service competes fairly in the provision of competitive products. *Id.* at 121. The order cites to the regulation at 39 C.F.R. § 3015.7 establishing the minimum contributions by competitive products to institutional costs as required under section 3633. *Id.* However, the minimum contribution to institutional costs is but one aspect of section 3633, *i.e.*, § 3633(a)(3), together with § 3633(b) requiring a 5 year review, whereas section 3633(a)(2) has a different purpose, to ensure each competitive product covers its costs attributable so that the Postal Service will not lose money on each piece of competitive product mailed.

The decision to utilize incremental cost methodology to calculate attributable costs bears directly on the application of subsection 3633(a)(2). The new methodology has the effect of increasing attributable costs, thereby affecting minimum competitive rates which potentially impact competition when ensuring that each competitive product covers its attributable costs under § 3633(a)(2), as well as a finding relating to the appropriate coverage of institutional costs under § 3633(a)(3). Order No. 3506 at 61.

Section 703 references all of section 3633, not only section 3633(b)(3) or section 3633(b). If Congress had meant to limit the requirement in section 703 to proceedings considering the proportion of institutional costs to be covered by competitive products under either section 3633(a)(3) or section 3633(b), it could easily have specified those subsections. Without such a limitation, Congress must have intended for section 703 to apply to any proceeding impacting attributable costs under section 3633(a)(2), as well as other subsections of sections 3633.

In reality, Order No. 3506 essentially modified the Commission's regulations under section 3633. Although the Order did not issue the rules proposed here to carry out the findings, nevertheless, the order itself directed the Postal Service to modify its reporting requirements to include inframarginal costs within attributable costs without

further delay. Order No. 3506 did not discuss the particular sections of the Commission's rules to be modified, but the Postal Service was directed to comply with the substantive principal regarding the inclusion of inframarginal costs to calculate attributable and incremental costs. This is substantiated by the comment in the Notice of this proceeding that while these are the only rules under title 39 requiring revisions as a result of Order No. 3506, the findings [in Order No. 3506] concerning incremental costs "applies to any reference of attributable costs in title 39 unless otherwise indicated by the rules." Notice at 6, citing see generally Order No. 3506.

Thus, the current state of competition was a relevant consideration when determining the appropriate costing make-up of attributable costs for competitive products. The incidental notation in Order No. 3506 that the change in the attribution of costs "reduces potential economic distortions" does not sufficiently serve as the consideration required by section 703. See Order No. 3506 at 122 n. 152. The footnote does not consider the net effect on competition due to the changes in laws since the FTC Report as required by section 703. The new methodology for calculating attributable costs impacts the final rates charged for competitive products and affects whether the rates cover attributable costs as required by section 3633(a)(2).

2. Section 703 in this rulemaking

The Notice in this docket lists 39 U.S.C. § 3633 as one of the statutory sections authorizing the proposed rules. Notice at 8. Although the proposed amendments in this docket merely implement the decisions made in Order No. 3506, because the Commission determined Order No. 3506 did not modify regulations under section 3633 and did not follow the requirements of section 703, the provisions of section 703(d) must apply to the proposed change in the regulations under section 3633 in this docket. The Commission cannot avoid the requirements of section 703. However, there is no indication in the Notice of any intent to consider section 703 issues.

3. Incorporation of Public Representative Comments in Docket No. RM2016-2

The comments in Docket No. RM2016-2 contained information and argument regarding the nature of competition between the Postal Service and private companies. Order No. 3506 summarized the comments and reply comments of participants on this issue. Order No. 3506 at 113-117. The Commission did not consider the nature of the competitive market in reaching its decision in Order No. 3506. *See Id.* at 117-124. That information should be reviewed in this proceeding. The Public Representative hereby incorporates by reference into these Comments, the Public Representative's Comments previously filed in Docket No. RM2016-2, January 27, 2016 at 7, 43-53; Public Representative Notice of Errata to Public Representative Comments, February 18, 2016, revised page 51; and Public Representative Reply Comments, March 25, 2016 at 28. To enable full consideration of this issue, other commenters may wish to incorporate additional portions of their comments from that proceeding into this docket for the Commission's consideration.

C. Suggested Style Modification of Section 3015.7(b)

In the event the Commission decides to implement the rules as proposed without modification, the Public Representative suggests a minor rearrangement of wording to the proposed rule in section 3015.7(b) for clarity and readability: move the last phrase in the second sentence, "to calculate attributable costs", to the front part of the sentence to read:

Pursuant to 39 U.S.C. 3631(b), to calculate attributable costs the Commission will use a competitive product's incremental costs, which is the sum of volume-variable costs, product-specific costs, and those inframarginal costs calculated as part of a competitive product's incremental costs.

IV. CONCLUSION

The Public Representative respectfully submits the foregoing comments for the Commission's consideration.

Respectfully submitted,

Kenneth E. Richardson
Public Representative

901 New York Avenue, N.W.
Washington, D.C. 20268-0001
(202) 789-6859; Fax (202) 789-6861
richardsonke@prc.gov